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The program assigns me a subject of fascinating vagueness, but my real topic is the reparation and inter-ally debt question, with particular reference to the so-called transfer problem.

It is nearly four years since the Dawes plan ushered in a real peace and made possible the resumption of normal processes of production and trade. Within that period, there has been a striking improvement in European conditions. But the time has been too short for any such substantial and permanent improvement to have occurred as would warrant the idea that the plan has completed its service to mankind. Its continued successful operation remains a matter of vital consequence to the political and economic stability of Europe, and thus, as one does not need to emphasize in this company, of large immediate importance to us in America.

The inter-ally debt settlements have an importance of a different kind. Except in the case of England, the period of large instalment payments has not yet arrived and the question of their direct economic effects is still one of the future. The settlements have, however, a large present significance in the influence which they exert on the reparation question. Simplifications of the machinery of the Dawes plan are now being suggested, having as desirable features the definite fixation of the German liability and the commercialization of the debt through the sale of reparation bonds to the world investing public for the benefit of the allies. But these suggestions are invariably linked with a proposal that Germany's obligation be fixed at a figure considerably lower than the estimated value of the present annuities, and a serious stumbling block immediately appears in the debts owed by the allies to this country. So long as those obligations in their present magnitude hang over the allies, it does not seem likely that we shall see any important revision of the plan involving further concessions to Germany.

Nor, in my view, is further concession by the allies necessary, either equitably or from an economic standpoint. The burdens resting on the allies are no less than those on Germany; and the idea that the reparation debt (or the inter-ally debts) must be reduced because of difficulties to be encountered in transferring payments across frontiers is without substantiation.

The record of the Dawes plan to date is one of unqualified success. Its prospects, fundamentally, are of the best. It is powerfully supported by public opinion, which, as we all know, is today much better informed and far more potent in international affairs than ever before in history. Public opinion is reasonably clear, and properly so, that the burden placed on Germany by the Dawes plan is an equitable one, that it is not based on the idea of revenge and that it has no reference to the tangled question of responsibility for the war. The burden is laid in the interest of a fair distribution of the war losses among all the nations of Europe, no one of which could undertake to carry a disproportionate load without involving all of them in the common danger of collapse. The French are pinning their hopes of rehabilitation to the Dawes plan; and the Germans, under the intelligent leadership of men like Marx, Stresemann and Luther, are able to recognize the benefits of political stability and economic reconstruction which the plan confers on Germany itself.

The Dawes plan is morally well grounded; and it was an advantageous settlement for all concerned. At bottom, therefore, it is sound and vigorous. We are told, however, by a school of English economists, that the plan is impractical. It works, but the Keynes school tells us that it cannot continue to work when the period of maximum payments arrives this fall. It is a fair and advantageous arrangement, drawn up, accepted and supported by reasonable and intelligent men. But the economists tell us that there is an economic law with which a settlement of such a character is in conflict, and which will compel the plan to give up the ghost. They tell us of a new economic something recently come into the laws of international exchange, called the transfer problem, which prevents a willing and solvent debtor from paying or a willing and needy creditor from receiving, without harm to himself, the installments on any international debt as large as the reparation debt.

This so-called transfer problem has been made the basis of repeated warnings to the French that they must reduce their reparation claims. The annuities provided under the Dawes plan I estimate have a capitalized value of nine billion dollars. Roughly half of the obligation runs to France. The French need the relief which it represents. Their struggle for fiscal and economic regeneration is scarcely yet out of its initial chapter, and they are wholly unreconciled to the idea of a stoppage of reparation payments. They take no stock in the transfer problem. They are deeply impressed by the view that if reparation payments should be suspended by the Transfer Committee, such action would occur not as a consequence of any inherent economic difficulty, but as a result of this very transfer agitation itself.

There can be no doubt that the predictions of a breakdown, unsubstantial though they are intrinsically, would tend, if given credence, to bring about that very catastrophe, just as the spread of unfounded rumors in the street has been known to cause a disastrous run on the deposits of a bank. There is a close similarity between the two cases. For the Dawes plan functions in a very real and definite sense as a part of the world credit system. Its operation today depends on the American investor. It is the dollar exchange being made available to Germany through American loans which furnishes the means of transferring the payments out of Germany. This process, at the present stage of the reconstruction of Europe, is a wholly natural and healthy one for all concerned, and in normal conditions it seems due to go on for a long time to come. But the Keynes school is determined that the American investor shall believe it to be a dangerous and unnatural process. If the investor should take these ideas seriously and stop loaning our surplus capital to Europe, the result undoubtedly would be a political and commercial crisis of considerable proportions, affecting this country, as well as Europe. The discoverers of the transfer problem are playing with forces of a highly explosive nature, both economic and political, and their ideas ought to be clearly recognized and tagged for what they are, a body of doctrinaire theory possessing no solid foundation.

These theories have had a considerable success with the man in the street. Under their influence former standards of judgment regarding the creation and payment of debts have become dowdy and old-fashioned. Those old standards, possessed of a certain fundamental simplicity and tested by long experience, regarded taxable capacity as the criterion relating to the creation and payment of government debt and industrial earning power as the criterion for commercial debt. But since the war, we have talked a new language—a kind of economic jargon. Nothing now seems to us worth noticing but the export surplus, failing to possess which, the debtor, we have been told, cannot pay, and succeeding in possessing which he will, by paying, bring serious embarrassment or ruin to the industrial life of the creditor nation.

Of such stuff is modern economic theory made. For nearly a decade the spectre of the export surplus has dominated the minds alike of those who have feared that the debts could not be paid and of those who feared that they would be paid. An economic law has been discovered, which though it did not operate at all before the war, is now said to operate with remorseless finality. It is a law which now runs to the disqualification of France as the principal creditor on reparation account and of the United States as the chief creditor on inter-ally and commercial loan accounts, but which, in pre-war days, when England was creditor on world account in nearly twice the amount of the present position of the United States, did not run at all.

Today, Europe and the rest of the world owe us on commercial debt about nine billion dollars (net after deducting American obligations owed to abroad); and on inter-ally debt, about seven billion dollars (representing the real present value of the annuities contemplated by the funding agreements, if capitalized at four per cent). The total is 16 billion dollars, the difference in the character of the two major components of this indebtedness being immaterial, so far as any possible difficulties of transfer are concerned. As against this 16 billion dollars owed to the United States at the present time, the United States and the rest of the world before the war owed Europe the equivalent of 50 billion dollars in present day values (our share being 7½ billions). Thirty billion dollars of this debt was owed to England alone and most of the remainder to France and Germany.

Now what happened in the matter of international debt collection in those pre-war years? What happened was that every solvent debtor paid his debts without difficulty to himself or anyone else, and every English investor who held foreign obligations of good credit rating regularly cashed his coupons and duly deposited his collections of matured principal in a sterling bank account or any other kind of a bank account in which he saw fit to place them. Individually, every good debt was collected in cash; the aggregate of the foreign lendings, however, never decreased. It increased steadily, other requirements of the industries of debtor countries taking the place of the obligations which were paid off. Nothing untoward happened in the realm of economic law, and the transfer problem was unheard of.

What new factor has, since the war, been introduced into the situation to change all this? What, if anything, has made the international economic system of the past suddenly sinister or unworkable? The answer is, of course, nothing at all. All that has happened is that Country X which was a creditor is now a debtor and Country Y which was a debtor is now a creditor. The transfer problem is nothing but a state of mind. When the inter-ally debts were suddenly and dramatically created in the amount of 10 billion dollars, 200 or 300 million people looked at them and gasped, and of that number not one-tenth of one percent had ever heard of the 50 billion dollars of foreign obligations (33 billions in pre-war values) which Europe had held in 1913. A legend of impossibility and danger was then and there created, which grew and spread and came to be widely accepted by many who have never to this day applied to it the critical test of experience and common sense.

The fact is that international debts normally never have been paid by means of an export surplus. International debts arise solely as a consequence of the fact that the debtor countries possess no export surplus; and over long periods of years they are paid, as they mature, by the creation of fresh debt. Nothing could be more natural, more healthy or more profitable for all concerned than the working out of this cycle of world distribution of capital. And nothing has been passed over in more complete silence by that school of British economists who looked at the inter-ally debts and solemnly pronounced them impossible.

The world is divided at any given time into natural debtor countries and natural creditor countries. A natural debtor country is one whose current needs for capital for internal development or reconstruction exceed its annual savings—thus the United States before the war and Europe today. A natural creditor country is one whose current needs for capital at home are less than its annual savings—thus Europe before the war and the United States today. And the index of these needs lies in interest rates. Capital follows interest rates as the tides follow the moon. It is obedient to the law of supply and demand; and so today our surplus capital, the product of our industries, loaned abroad by our investors, is flowing across the Atlantic in a steady stream.

This movement of the capital of a creditor country, these shipments of its surplus production constitute the only authentic export surplus known to the international economic system—the export surplus which a natural creditor nation inevitably has and which a natural debtor nation inevitably has not. The authentic export surplus moves not *from* but *to* the debtor nation. After the primary exchanges of goods against goods have taken place to the full extent of the natural debtor country's exports, the secondary movement of trade takes place—that significant movement of the export surplus of the natural creditor against securities of the natural debtor, profitably employing the excess productive capacity of the creditor and building up the deficient capacity of the debtor. In this manner, and in this manner only, are international debts (on balance) created, and, so long as the debtor remains a natural debtor, are the interest and sinking fund charges on them settled.

For ten years British economists have been dinning into our ears that Germany and the allies cannot within a considerable time be expected to develop an export surplus. This demonstration has been a work of supererogation, for it is obvious that Europe's losses cut untold billions deep into her productive powers, as measured by plant, good will and manpower. But the idea that without an export surplus those countries cannot settle their international balances in a wholly natural way for an indefinite period has nothing to support it.

Trade and finance under the modern system and on the modern scale came into being in the last century, and throughout that century the normal and only method of payment of international debts was through refunding, not in detail, but in the aggregate. Never, except on the abnormal occasion of a complete world overturn and then only for the four years duration of the overturning process were international debts ever settled through an export surplus. That occasion was when, under the stimulus of an unheard of war demand and after years of intensive development as a debtor nation, the United States took its new position in the world, settled its accumulated balance by a huge export of goods to Europe, and created a balance of 10 billion dollars on the other side of the account. Normally, international capital balances are never finally settled at all, any more than are the deposits of the banks or the obligations of the railroads. Once only in history has such a settlement of international balances ever taken place, and then only at the end of a cycle—the end, so far as we can now see, of the cycle of European economic supremacy and the beginning of the cycle of American supremacy.

The aggregate indebtedness keeps piling up. Individual debts are paid, but new ones, on an increasing scale, commensurate with the expansion of population and the natural growth of business, take their place. The dollar exchange created by the new loans takes care of the old loans and finances new American exports. And so the process goes on in this new world job of ours, which England once performed. This expansion, the English tell us, is dangerous to the United States. But I have yet to hear any sensible reason advanced why it is dangerous or why it cannot go on indefinitely to levels scarcely yet dreamed of. And, as a practical matter, at the present rate of increase, which for the year 1926 was about 700 million dollars, net after offsets for money loaned to us, it will be 50 years before we arrive at that position which European manufacturers and investors held in world trade and finance in 1913.

It seems to me that on the evidence, we may safely conclude that those who have feared that the debts, whether reparation, inter-ally, or commercial, cannot be paid because the debtor countries will not have an export surplus, have been unnecessarily concerned. For, so long as the debtor countries have no export surplus, they will be in the market for new foreign loans, and the debts will be paid by the new loans. And, when, by the aid of the loans and other natural recuperative processes, those countries have built up their productivity and come to the point of being natural creditor nations, with export surpluses of their own, the debts will then be paid by means of export surpluses. Obviously, a nation must either have an export surplus or not have one, and under neither condition has any economic law of attainder running against creditors ever yet been passed.

With the same facts in mind regarding the world ebb and flow of surplus capital there is, I think, a brief and relatively simple answer to the apprehensions of those who fear that the debts owing to us will some day be collected by means of a European export surplus and that our industries will be buried under the influx. The picture which they draw of a huge increase in our imports brought about by the pressure of debts seeking to be paid, is nothing more than a figment of the imagination. The debts, whether they be big or little, will be a merely passive factor in the situation.

If, in the future, we should become a natural debtor country by comparison with Europe, that is to say, needing capital more acutely than Europe and accordingly offering higher interest return for it, that condition will not arise for reasons connected with the existence of the debts nor will its degree be at all proportionate with their size. It will arise, if it arises at all, from the need of more capital at home and it will presumably be satisfied in the first instance by keeping our export surplus at home, and after that, if we need still more capital, by demanding Europe's surplus. In such circumstances, our industries will be crying for capital, they will be crying for increased productivity, and the resulting import of capital goods, which industry itself will voluntarily stimulate by offering high interest rates, will serve the dual purpose of providing new capital and of supplementing a shortage of home product. In this process, the debts will be collected against the deficiency in our export balances, but they will have no part in creating that deficiency. When this condition begins to run, we shall be collecting the debts by exporting the evidences of debt, and, so far as I can see, the only significance which the size of the debts will have will be that the more foreign obligations which we hold, the longer will it be before we begin to export our own obligations in settlement of our adverse current balances.

The sum and substance of the matter, so far as supposed dangers of debt collection in goods are concerned, is this: That if we do in the future decrease our exports and increase our imports it will be for reasons unrelated to the debts and connected solely with the matter of capital supply and demand, in circumstances which we in the past as a debtor nation and Europe in the present as a debtor continent have found to be thoroughly healthy and stimulating.

But who is there who thinks that this situation is going to arise soon or suddenly? Whether its possibilities relate only to the satisfaction of natural and complementary demands of the nations concerned, or whether they contain also elements of danger, we may safely agree with the economists as to the unlikelihood of Europe's soon producing an export surplus. Can we not then for the present enjoy at its full artistic value, without indulging in too many anticipatory shivers, their thrilling depiction of what will one day happen when American industry in the role of Little Red Riding Hood comes face to face with the ugly fangs of Europe's Export Surplus?

Naturally, by our loans we are building up the productive strength of our competitors. But shall we be frightened by our own prosperity? If we wish to trade and prosper today we cannot help benefiting Europe by the rich and fertile overflow of our surplus, even if we would. And if as a nation we would prevent it if we could, we should be guilty of the twin stupidities of failing to recognize Europe as more of a customer than a competitor and of failing to understand that the healthy activity even of a competitor builds wider markets everywhere for all.

As for the inter-ally debts, it is too late to consider them at all in such a significance. If they conserved Europe's basic productivity by helping to preserve Europe's liberties that was all done and completed a decade ago when the loans were made. And it would be ridiculous for us to cancel them for fear of the hobgoblin labelled dangers of repayment. It is inconceivable that the American people would be willing to place themselves in history as the butts of such a colossal hoax. If we decide to reduce the debts further we ought to do it on grounds creditable to our intelligence and meriting the respect of the world, as an act of human forbearance, of political sagacity and, as I see it, of business sense. I am not here to argue revision of the debt settlements. I should like merely to suggest that the real outlines of the question have so far been obscured by a fog of pseudo economic doctrine. When that is cleared away, we shall perhaps be able to consider whether it is worth our while in spiritual satisfaction to secure the good will of Europe's overburdened taxpayers, and whether an increase in their purchasing power would be profitably reflected in our export trade.

Whatever our decisions on this and other questions related to the subject of international debts we might appropriately celebrate our entry into wider fields of world affairs by declaring our independence of doctrinaire economics and assinging a somewhat higher value, than is now the fashion, to judgments based on experience.